

Comments on Retirement Committee's Draft Request for Proposals for NDPERS Retirement Plan Design Study

Prepared for: Rep. Mike Lefor, North Dakota House of Representatives

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The Pension Integrity Project at Reason Foundation offers pro-bono technical assistance to public officials and other stakeholders to help them design and implement policy solutions aimed at improving plan resiliency and promoting retirement security for public employees. The Project has served as lead technical advisors on a wide range of recent, bipartisan public retirement system reforms in states including Texas, Michigan, Arizona, Colorado, New Mexico and more. We are happy to share that experience with the Retirement Committee throughout the interim to help inform your current process and find consensus that balances the interests of stakeholders and taxpayers.

The Pension Integrity Project commends the diligence with which the Retirement Committee is approaching its analysis of potential changes to the current NDPERS offerings for state and municipal government employees, per the charge outlined in House Bill 1209 from the 2021 regular session. These are important public finance issues with major long-term fiscal implications for the state as well as NDPERS members of all kinds, and the situation should be approached with robust analysis, deliberation, and stakeholder dialogue.

To that end, our review of the draft request for proposals (RFP) prompted two key observations—and accompanying suggested changes—that we believe may improve the robustness of the analysis that will ultimately be provided by the selected consultant.

1. Long-term pension analysis generally benefits from the use of sensitivity analysis to understand how changes in one key variable affect the underlying actuarial findings. One of the most important variables to understand is the discount rate (which is typically also the assumed rate of return of the pension system). Given the diminishing capital market forecasts from major investment firms—along with the consistent moves by similar pension systems across the country in recent months to lower their assumed rates of return accordingly—we recommend that the Committee request that the consultant provides actuarial forecasts at both the current NDPERS discount rate and a lower rate tied to long-term US Treasury yields with a risk premium included.
2. States like Florida, Michigan, Arizona, and Colorado have all embraced a “middle ground” option over the last decade that eschews picking a “one-size-fits-all” option (e.g., defined benefit pension, defined contribution plan, hybrid, etc.) altogether, and instead offers new employees a choice in retirement benefit. For example, employees hired after a certain future date could choose between a default primary defined

contribution retirement plan or a new, risk-managed tier within the existing defined benefit pension system. This new tier would be designed to bear lower/no financial risk for employers and taxpayers, while ensuring that current legacy unfunded liabilities are paid off on the same (or faster, preferably) schedule as today.

Suggested revisions to this effect are offered below for Section 1 of the RFP, shown in *red italics*:

1. Actuarial estimates, including:

a. The unfunded liability of the plan as it currently exists, identifying the state's share of the unfunded liability and each participating political subdivision's share of the unfunded liability, *as valued at both:*

- *the current NDPERS discount rate; and*
- *a discount rate that is 200 basis points above a three-year rolling average of the 20-year US Treasury constant maturity rates as of June 30 of the previous fiscal year.*

b. The unfunded liability if the plan is closed to new hires effective January 1, 2024, and new hires participate in the state's existing or modified defined contribution plan, identifying the state's share of the unfunded liability, and each participating political subdivision's share of the unfunded liability. This analysis should value those unfunded liabilities *at both:*

- *the current NDPERS discount rate; and*
- *a discount rate that is 200 basis points above a three-year rolling average of the 20-year US Treasury constant maturity rates as of June 30 of the previous fiscal year.*

c. The amount of a lump sum cash deposit into the plan on July 1, 2025, to enable the plan to be 100 percent funded in 20 years—*on both a level percent of payroll amortization and level dollar amortization basis*—for:

(1) The plan as it currently exists, identifying the cash infusion necessary for the state's portion of the plan and the cash infusion necessary for the political subdivision's portion of the plan; *and*

(2) The plan if closed to new hires effective January 1, 2024, identifying the cash infusion necessary for the state's portion of the plan and the cash infusion necessary for each political subdivision's portion of the plan; *and*

(3) *The plan if closed to new hires effective January 1, 2024, but subject to the following conditions:*

- *All new state employee hires on or after January 1, 2024 are defaulted into the current NDPERS optional defined contribution plan at current contribution rates*
- *All new state employee hires on or after January 1, 2024 are offered the choice of not joining the default defined contribution plan and selecting an alternative NDPERS pension design that:*

- *Represents a new tier within NDPERS for state employees hired on or after January 1, 2024;*
 - *Utilizes the current pension accrual rate (multiplier), but for which the new tier of employees is capped at no higher than a 6% discount rate to mitigate risk in the new pension tier, and*
 - *Includes a cost sharing mechanism whereby employers and new-tier employees share all normal cost and any future, new-tier unfunded liability amortization payments on an equal (e.g., 50/50) cost-sharing basis.*
 - *Continues to amortize legacy NDPERS unfunded liabilities over total payroll—meaning payments are calculated on all legacy tier and new tier employees alike.*
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We hope this information is useful and we welcome any related questions or dialogue with the Committee. Please let us know if you have any questions or need additional information.

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